

2010 federal budget indicates likely tax policies

On April 29, 2009, both houses of the U.S. Congress passed budget resolutions for 2010. Included in the \$3.56 trillion budget are several tax-related items that could affect both individual and business taxes. While the tax items in the budget resolution are nonbinding, it does highlight the tax policies likely to be considered by Congress in the near future.

Tax Relief

Alternative Minimum Tax (AMT) relief

The budget calls for relief from the AMT tax for three years. For the past few years, Congress has attempted to alleviate the spread of the AMT tax by temporarily increasing the AMT exemption amount. For 2009, the AMT exemption amount is \$46,700 (\$70,950 married filing joint). However, these “patches” would expire and the AMT exemption would fall back to a significantly lower amount (\$33,750 for single filers and \$45,000 for married filing joint), causing more taxpayers to be subject to AMT. The 2010 budget would patch the AMT for three years by keeping the exemption amounts the same as the 2009 exemption indexed for inflation.

Extension of the 10% tax bracket

The 10% marginal tax bracket was originally enacted in 2001 under the *Economic Growth and Tax Relief Reconciliation Act* (the 2001 Act). The 10% bracket was carved out of the previous 15% tax

bracket, which prior to 2001 was the lowest tax bracket. For 2009, the 10% bracket applied to a taxpayer’s first \$8,350 of taxable income (\$16,700 married filing joint). Without further legislation, the 10% bracket would revert back to 15% after 2010. The budget proposes to permanently extend the 10% tax bracket for tax years after 2010.

Extension of other tax rates for middle-income taxpayers

In addition, to the creation of the 10% marginal tax bracket, the 2001 Act also reduced the former tax brackets (15%, 28%, 31%, 36% and 39.6%) to the following brackets: 15%, 25%, 28%, 33% and 35%. Similar to the 10% bracket, the reduced brackets are scheduled to expire and revert to the former marginal tax rates for tax years after 2010. The budget proposes to permanently extend the 15%, 25% and 28% brackets for tax years after 2010 for families making less than \$250,000. In addition, the preferential rate on long-term capital gains and

qualified dividends would be extended for families making less than \$250,000.

Estate Tax Relief

Because of the 2001 Act, the estate tax exemption level has steadily increased and the highest estate and gift tax rate has decreased. For 2009, the estate exemption level is \$3.5 million (\$7 million for couples) and the highest estate and gift tax rate is 45%. The 2001 Act completely repeals the estate tax for decedents dying after December 31, 2009. However, the estate tax returns in 2011 under the sunset provisions of the 2001 Act. The pre-2001 estate tax exemption level and top estate tax rates also would return (\$1 million exemption and a top estate and gift tax rate of 55%). The 2010 budget proposes to make the 2009 estate tax exemption level and rates permanent.



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Revenue raisers

Additional funding for Internal Revenue Service enforcement

To help offset the costs of the various tax-relief measures provided in the budget, Congress plans to increase appropriations for IRS enforcement activities by \$387 million to \$5.5 billion for 2010. The increased appropriation is intended to help close the “tax gap” (*i.e.*, difference between what is owed by taxpayers and what is actually collected) through stepped-up enforcement activities by the IRS.

Increase in top two marginal tax rates

As previously discussed, the budget proposes to permanently extend the 10%, 15%, 25% and 28% marginal tax brackets for middle-income taxpayers. However, the budget would let the top two marginal rates of 33% and 35% expire after 2010

and revert back to the pre-2001 rates of 36% and 39.6%.

Other revenue raisers

In addition, the budget includes \$97 billion in tax loophole closers to be determined by the Senate Finance Committee and the House Ways & Means Committee. While the budget does not provide any examples of potential revenue raisers, several items were discussed in President Obama’s budget proposal released earlier this year. These proposed revenue raisers included the following:

- Repeal of the Last In, First Out (LIFO) method for inventory
- Tax carried interest as ordinary income
- Repeal the domestic production activities deduction for oil and natural gas companies

- Repeal percentage depletion for oil and natural gas
- Repeal expensing of intangible drilling costs for oil and gas companies
- Increased enforcement in the international tax area and international tax reform policies

To learn more about the impact of the proposed budget on you and your business, contact your BKD advisor.

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